NO. 85556-1

SUPREME COURT
OF THE STATE OF WASHINGTON

TESORO REFINING AND MARKETING COMPANY,

Respondent,

v.

STATE OF WASHINGTON,
DEPARTMENT OF REVENUE,

Petitioner.

BRIEF OF AMICUS CURIAE DOT FOODS, INC.

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I. STATEMENT OF INTEREST OF AMICUS CURIAE

Dot Foods, Inc. ("Dot Foods"), is an Illinois wholesaler of consumer products. Dot Foods structured its sales operations so as to qualify for the direct seller's representative ("DSR") exemption from B&O tax under RCW 82.04.423. This Court affirmed Dot Foods' eligibility for the DSR exemption under the "unambiguous" terms of the statute in *Dot Foods, Inc. v. Dep't of Revenue*, 166 Wn.2d 912, 926, 215 P.3d 185 (2009).

In 2010, in legislation remarkably similar to the 2009 amendments at issue in the appeal of Tesoro Refining and Marketing Company ("Tesoro"), the Legislature passed a bill stating that the original intent of RCW 82.04.423 (enacted in 1983) was narrower than and inconsistent with the result in *Dot Foods*, 166 Wn.2d 912, and asserting that its purpose was to amend the statute "retroactively to conform the exemption to the original intent of the legislature." Laws of 2010, 1st Sp. Sess., ch. 23, § 401(4) (enacting Second Engrossed Substitute Senate Bill 6143 ("2ESSB 6143")).

Sections 402 and 1704 of 2ESSB 6143 amended RCW 82.04.423 retroactively to match the arguments made by the Department of Revenue in *Dot Foods*. Section 402 also repealed the DSR exemption prospectively. *See* Appendix A (Sections 401, 402, 1704, and 1706 of 2ESSB 6143).

The 2010 legislation apparently sought to avoid certain legal issues by preserving, in isolation, the decision of this Court in the *Dot Foods* case. Section 1706 of the act provided that "Section 402 of this act does not affect any final judgment, not subject to appeal, entered by a court of competent jurisdiction before the effective date of this section." While one might assume that this language preserved Dot Foods from any harm resulting from the retroactive legislation, in fact the Department has declined to give the judgment any effect after the end of the tax periods squarely before this Court in *Dot Foods*. Specifically, the Department has refused to grant refunds to Dot Foods for the open periods after the refund periods at issue in *Dot Foods* (that is, beginning May 2006), including those periods prior to the date of this Court's decision. *See* Letter from A. Van Gerpen, Department of Revenue, to B. Metzinger (July 2, 2010) (copy at Appendix B). The Department also assessed Dot Foods additional B&O tax for the period following this Court's decision and before the effective date of 2ESSB 6143. *See* Examiner's Detail of Differences and Instructions to Taxpayer at 3 (copy at Appendix C).

Dot Foods faces a retroactive deprivation of statutory tax relief under an "unambiguous" statute exactly like Tesoro – only worse, since the statute's "plain meaning" was already determined by this Court. Dot Foods therefore has a strong interest in the Court's Due Process analysis in this case.[1]

[1] Dot Foods paid the assessment discussed in Appendix C and sought a refund for the periods of May 2006 through April 2010 in Thurston County Superior Court. Dot Foods

II. ARGUMENT

A. The Department's Argument Combines Due Process and Separation of Powers Cases in a Misleading Way.

The Department petitioned this Court to review whether the retroactive 2009 amendment of RCW 82.04.433 deprived Tesoro and others of property without due process of law. Pet. for Review at 1 (Issue 2). The Department's argument to this Court, however, relies only in part on Due Process cases. The Department also relies in part – if not primarily – on cases addressing whether a retroactive statute exceeds legislative power, under separation of powers doctrine or in general. *See* Supplemental Br. of Pet'r at 14-18.[2] The Department does not call the Court's attention to this fact. The briefing in this Court echoes the Department's argument below. *See* Br. of Resp't at 34-46.

As this Court knows well, Due Process and separation of powers doctrines are not the same. Their concerns are different and the tests for compliance are different.

Due Process protects private persons from "arbitrary and irrational legislation." *United States v. Carlton*, 512 U.S. 26, 30 (1994) (quoting *Pension Benefit Guar. Corp. v. R.A. Gray & Co.*, 467 U.S. 717, 733

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claimed relief on Due Process grounds particular to its case and on other, independent grounds. The case is stayed pending this Court's decision in the instant appeal.

[2] These cases include *Hale v. Wellpinit Sch. Dist. No. 49*, 165 Wn.2d 494, 507-08, 198 P.3d 1021 (2009) (*see* Supplemental Br. of Pet'r at 17-18), *Washington State Farm Bureau Fed'n v. Gregoire*, 162 Wn.2d 284, 174 P.3d 1142 (2007) (*see* Supplemental Br. of Petitioner at 14-15, 18), *Port of Seattle v. Pollution Control Hearings Bd.*, 151 Wn.2d 568, 90 P.3d 659 (2004) (*see* Supp. Br. of Petitioner at 15), and *McGee Guest Home, Inc. v. Dep't of Soc. & Health Serv.*, 142 Wn.2d 316, 12 P.3d 144 (2000) (*see* Supplemental Br. of Pet'r at 15).

(1984)). Under federal law a retroactive tax statute will be upheld against a Due Process challenge if it "is supported by a legitimate legislative purpose furthered by rational means." *Id.* at 30-31 (quoting *Pension Benefit*, 467 U.S. at 730). But, as the Supreme Court's opinion illustrated, an otherwise legitimate purpose may be tainted by an illegitimate purpose (such as targeting a specific taxpayer's claims, *id.* at 32) and that rationality of the chosen means is contingent on circumstances (such that a retroactive change for a period that is more than "modest" in length, given the practicalities of the legislative process, is not rational, *id.*). Furthermore, Washington cases have determined the question of arbitrariness largely by insisting on a short period of retroactivity, *see* Supplemental Br. of Resp't at 10-14 (discussing cases), which may be relaxed in the rare case where taxpayers are afforded a constitutional remedy for an illegal tax for the entire period in question. *See W.R. Grace & Co. v. Dep't of Revenue*, 137 Wn.2d 580, 599-600, 973 P.2d 1011 (1999) (discussed further below).

By contrast, the separation of powers doctrine, when addressing the question whether the Legislature has exceeded its powers, does not ask whether the Legislature had a legitimate purpose or whether the legislation itself was rational. Instead, the issue is whether the Legislature has intruded on a judicial function or threatened the "independence, integrity, or prerogatives of the judicial branch." *Lummi Indian Nation v. State*, 170 Wn.2d 247, 262, 241 P.3d 1220 (2010) (citing *Hale v. Wellpinit Sch. Dist.*

No. 49, 165 Wn.2d 494, 507-08, 198 P.3d 1021 (2009)). A retroactive statute might not intrude on a judicial function, and lie within the legislative power as such, but still impose an irrational or arbitrary injury on private persons and be unconstitutional on that ground.

Consequently, the Department's reliance on cases relating only to the legislative power to enact retroactive legislation is misplaced. The quotations pulled from these opinions do not defeat or even bear on Tesoro's Due Process claims. This is not to concede that a latent separation of powers issue is absent from this case – it has just not been presented by the parties.

B. The Department Relies on Inapposite Cases Involving Ambiguous Statutes or Complicated Extenuating Circumstances.

None of the cases in which the Department finds support is like Tesoro's case, where the Legislature jumped in to "clarify" a simple tax deduction 24 years after enactment when, at a moment of fiscal stress in state government, Tesoro sought a refund and parity with the treatment granted to other taxpayers. Instead, the Department relies solely on cases in which this Court expressly found that the preexisting statute was ambiguous or in which there was a complicated history concerning the preexisting statute. The Department's cases are not germane to this case.

First, the Department's one Due Process case, *W.R. Grace*, involved a completely different setting, as discussed by Tesoro, Appellant's Reply Br. at 31. That case involved challenges to the

retroactive remedy adopted by the Legislature after the U.S. Supreme Court invalidated the former multiple activities exemption of the B&O tax in *Tyler Pipe Industries, Inc. v. Washington State Dep't of Revenue*, 483 U.S. 232 (1987). *Tyler Pipe* was one of a series of Commerce Clause cases in the 1980s in which the Supreme Court was working out the logic of the new "internal consistency" test developed in *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159, 163 (1983). *See American Trucking Ass'ns v. Scheiner*, 483 U.S. 266, 283 n.14 (1987) (citing *Tyler Pipe*, 483 U.S. at 247; *Armco Inc. v. Hardesty*, 467 U.S. 638, 644-45 (1984); and *Container*, 463 U.S. at 163).

The Supreme Court found in *Tyler Pipe* that the multiple activities exemption worked a discrimination against interstate commerce, even though the same provision had been *validated* by the Court previously under its prior tests in *General Motors Corp. v. Washington*, 377 U.S. 436 (1964). The Supreme Court even offered Washington a simple fix for the constitutional defect: "[A]n expansion of the multiple activities exemption to provide out-of-state manufacturers with a credit for manufacturing taxes paid to other States would presumably cure the discrimination." *Tyler Pipe*, 483 U.S. at 249.

Given that the Legislature then adopted this credit remedy as specifically suggested by the U.S. Supreme Court, *see W.R. Grace*, 137 Wn.2d at 601, this Court saw no need to address either of the "legitimate purpose" or the "rational means" prongs of the *Carlton* analysis.

Taxpayers were not required to pay more under the new multiple activities credit than they had under prior law, which indeed had been validated previously by the U.S. Supreme Court.

The other cases cited by the Department are similarly complicated and different from Tesoro's case. In *Hale*, the retroactive amendment added a definition of the term "disability" to the Washington Law Against Discrimination where previously one had been lacking, and the context was that this Court had interpreted the term in two different ways in the span of six years. In *Washington State Farm Bureau Fed'n v. Gregoire*, 162 Wn.2d 284, 174 P.3d 1142 (2007), the issue involved one statute's implementation of a single fiscal year's expenditure limits under the often amended Taxpayer Protection Act in a manner different from the prior statute's procedure. In *Port of Seattle v. Pollution Control Hearings Bd.*, 151 Wn.2d 568, 90 P.3d 659 (2004), this Court held that the Legislature's retroactive ratification of an agency's methods for certifying water quality in connection with the Sea-Tac airport's third runway did not intrude on the judicial function. In *McGee Guest Home, Inc. v. Dep't of Soc. & Health Services*, 142 Wn.2d 316, 12 P.3d 144 (2000), this Court held that a pre-existing provision of the Administrative Procedure Act was ambiguous and that the Legislature's retroactive clarification in response to a trial court decision was within its power.

None of these precedents legitimize or justify any alleged attempt to clarify a statute that was in fact unambiguous.

C. "Clarifying" an Unambiguous Statute and Asserting Knowledge of Legislative Intent Across Decades Are Not Rational Means for Avoiding Tax Refunds.

The Department belittles the Court of Appeals' statement that the 2009 amendment entailed a 24-year retroactive change in RCW 82.04.433, *see* Supplemental Br. of Pet'r at 16 (citing *Tesoro Ref. & Mktg. Co. v. Dep't of Revenue*, 159 Wn. App. 104, 116, 246 P.3d 211 (2010)), but the fact that the Legislature sought to "clarify" a 24-year-old statute *ab initio* is a critical factor in resolving the Due Process issue.

All of the Washington and U.S. Supreme Court Due Process cases discussed by the parties dealt with a retroactive, express, and unambiguous change in the scope of a tax.[3] *See Carlton*, 512 U.S. at 29 (amendment imposing new, retroactive (14 months) ownership requirements for entitlement to deduction); *Welch v. Henry*, 305 U.S. 134 (1938) (imposing retroactive (two years) tax on dividends received from in-state corporations); *Japan Line, Ltd. v. McCaffree*, 88 Wn.2d 93, 94-95, 97-98, 558 P.2d 211 (1977) (imposing new, retroactive (two months) leasehold excise tax in place of prior property taxation of leasehold interests in public property); *Bates v. McLeod*, 11 Wn.2d 648, 655, 120 P.2d 472 (1941) (imposing new, retroactive (2.5 months) tax to support unemployment compensation); *State v. Pacific Tel. & Tel. Co.*, 9 Wn.2d 11, 16-17, 113 P.2d 542 (1941) (expanding use tax retroactively (four

[3] *W.R. Grace* is an outlier from this group, as discussed above, given that it did not involve a substantial change in actual tax liabilities but rather a retroactive remedy for a technical Commerce Clause violation.

years) to cover use of property acquired out-of-state).[4] In none of these cases did the court approve a retroactive period longer than two years. In all three cases where the retroactive expansion of tax liability was approved, the court specifically relied on the practical exigencies of the legislative process in addressing a prior legislative error, an area of confused tax administration, or the limited period between one session and another. *See Carlton*, 512 U.S. at 32; *Welch*, 305 U.S. at 150-51; *Japan Line*, 88 Wn.2d at 97-98. These are the types of considerations that ensure that a retroactive change in tax law is a rational means for furthering the goal of state revenue production.

The Legislature is presumed to know and act in consideration of this preexisting body of law. *See Price v. Kitsap Transit*, 125 Wn. 2d 456, 463, 886 P.2d 556 (1994) (citing authorities). The text of the 2009 act admits that the Legislature did not intend to enact an affirmative change, as was done in the foregoing cases, and it must be assumed that this choice was made to avoid setting an explicit period of retroactivity that would be tested against Due Process analysis. Instead, the Legislature presumed to act on the asserted fact that its 1985 enactment of RCW 82.04.433 was ambiguous and to stretch its "clarification" back 24 years to the original enactment. This approach is arbitrary and irrational both because RCW

[4] In *Pacific Tel. & Tel. Co. v. Henneford,* 195 Wash. 553, 560-62, 81 P.2d 786 (1938), this Court had held that the prior text of the use tax statute unambiguously excluded from tax any articles that were purchased out-of-state and were unavailable for purchase inside the state. *Compare Dot Foods, Inc. v. Dep't of Revenue*, 166 Wn. 2d at 926. It was in response to the 1938 *Pacific Tel. & Tel.* case that the Legislature enacted the four-year retroactive change at issue in *State v. Pacific Tel. & Tel., supra.*

82.04.433 was not ambiguous, as the court held below, and because the Legislature's claim that it knows the intent of legislators a full generation earlier is itself irrational.

The Legislature in this case (24 years after enactment), and with regard to the DSR exemption (27 years after enactment), has asserted essentially that imprecision in statutory drafting by a prior generation has led to consequences not intended by *them*. *See* Laws of 2009, ch. 494, § 1; 2ESSB 6143, § 401. As a question of cognition, it is unbelievable. As a matter of history, it is simply *ipse dixit*.

The Supreme Court's decision in *Carlton* shows that a claim of "unintended consequences" will support a retroactive change or clarification only when the difference between legislative goals and actual results are readily apparent to roughly the same body of legislators that enacted the original statute. *Carlton* emphasized how the IRS promptly informed Congress of the perceived error in the statute in question, 512 U.S. at 33, and how the corrective measure was then promptly introduced and passed, *id.* at 32. This process, in which taxpayers and the administrative agency test the consequences of a new tax statute, provides an appropriate context for legislative review and correction, if indeed unintended consequences arise.

This process justifies a "modest period of retroactivity," *id.*, that is rationally balanced against citizens' interest in finality and equality in tax treatment. *Cf. id.* at 37-38 (O'Connor, J., concurring). The Legislature's

action in this case, by contrast, is an abuse of this balance. To allow the Legislature license to "correct" "unintended consequences" in this case – more than two decades after the original enactment, during which time the Department consistently and expressly endorsed Tesoro's interpretation of the statute – would enshrine the use of fictional history as a rational means for furthering the Legislature's budgetary purposes.

If the Legislature wishes to amend a tax statute retroactively, Due Process requires that the Legislature state the period of retroactivity explicitly and that this period reflect the practical legislative circumstances associated with promptly addressing the particular problems in the prior statute. *See Carlton*, 512 U.S. at 31-32. This did not occur in this case, where the Legislature instead tried an end-run past the Due Process Clause – itself an arbitrary and irrational means of furthering its purposes.

III. CONCLUSION

For the foregoing reasons, Dot Foods requests that the Court affirm the judgment of the Court of Appeals.

RESPECTFULLY SUBMITTED this 12th day of September, 2011.

Davis Wright Tremaine LLP
Attorneys for Amicus Curiae Dot Foods, Inc.

By _____
Dirk Giseburt
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APPENDIX A

CERTIFICATION OF ENROLLMENT

SECOND ENGROSSED SUBSTITUTE SENATE BILL 6143

Chapter 23, Laws of 2010

61st Legislature
2010 1st Special Session

TAXES

EFFECTIVE DATE: Various

Passed by the Senate April 12, 2010
YEAS 25 NAYS 21

BRAD OWEN

President of the Senate

Passed by the House April 10, 2010
YEAS 52 NAYS 44

FRANK CHOPP

Speaker of the House of Representatives

Approved April 23, 2010, 1:44 p.m.

CHRISTINE GREGOIRE

Governor of the State of Washington

CERTIFICATE

I, Thomas Hoemann, Secretary of the Senate of the State of Washington, do hereby certify that the attached is **SECOND ENGROSSED SUBSTITUTE SENATE BILL 6143** as passed by the Senate and the House of Representatives on the dates hereon set forth.

THOMAS HOEMANN

Secretary

FILED

April 23, 2010

Secretary of State
State of Washington

SECOND ENGROSSED SUBSTITUTE SENATE BILL 6143

AS RECOMMENDED BY THE CONFERENCE COMMITTEE

Passed Legislature - 2010 1st Special Session

State of Washington 61st Legislature 2010 Regular Session

By Senate Ways & Means (originally sponsored by Senator Prentice)

READ FIRST TIME 03/06/10.

AN ACT Relating to modifying excise tax laws to preserve funding for public schools, colleges, and universities, as well as other public systems essential for the safety, health, and security of all Washingtonians; amending RCW 82.04.220, 82.04.2907, 82.04.2907, 82.04.460, 82.04.080, 82.32.090, 82.12.020, 82.45.033, 82.45.070, 82.45.080, 82.45.100, 82.45.220, 43.07.390, 82.04.4292, 82.04.423, 82.04.4266, 82.04.4266, 82.04.260, 82.04.250, 82.04.250, 82.04.250, 82.04.298, 82.04.334, 82.04.4463, 82.04.4463, 82.08.806, 82.32.550, 82.45.195, 35.102.150, 48.14.080, 82.08.890, 82.12.890, 82.04.360, 82.32.145, 82.08.0293, 82.08.0293, 82.12.0293, 54.28.011, 82.04.4451, 82.32.045, 82.04.394, 82.04.394, 66.24.290, 82.08.037, 82.12.037, 82.08.---, and 82.12.---; reenacting and amending RCW 82.45.010, 82.04.260, 82.04.261, and 82.04.440; adding new sections to chapter 82.04 RCW; adding new sections to chapter 82.32 RCW; adding new sections to chapter 82.08 RCW; adding new sections to chapter 82.12 RCW; creating new sections; providing effective dates; providing expiration dates; and declaring an emergency.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

PART IV

Direct Seller Business and Occupation Tax Exemption

NEW SECTION. **Sec. 401.** (1) A business and occupation tax exemption is provided in RCW 82.04.423 for certain out-of-state sellers that sell consumer products exclusively to or through a direct seller's representative. The intent of the legislature in enacting this exemption was to provide a narrow exemption for out-of-state businesses engaged in direct sales of consumer products, typically accomplished through in-home parties or door-to-door selling.

(2) In *Dot Foods, Inc. v. Dep't of Revenue*, Docket No. 81022-2 (September 10, 2009), the Washington supreme court held that the exemption in RCW 82.04.423 applied to a taxpayer: (a) That sold nonconsumer products through its representative in addition to consumer products; and (b) whose consumer products were ultimately sold at retail in permanent retail establishments.

(3) The legislature finds that most out-of-state businesses selling consumer products in this state will either be eligible for the exemption under RCW 82.04.423 or could easily restructure their business operations to qualify for the exemption. As a result, the legislature expects that the broadened interpretation of the direct sellers' exemption will lead to large and devastating revenue losses. This comes at a time when the state's existing budget is facing a two billion six hundred million dollar shortfall, which could grow, while at the same time the demand for state and state-funded services is also growing. Moreover, the legislature further finds that RCW 82.04.423 provides preferential tax treatment for out-of-state businesses over their in-state competitors and now creates a strong incentive for in-state businesses to move their operations outside Washington.

(4) Therefore, the legislature finds that it is necessary to reaffirm the legislature's intent in establishing the direct sellers' exemption and prevent the loss of revenues resulting from the expanded interpretation of the exemption by amending RCW 82.04.423 retroactively to conform the exemption to the original intent of the legislature and by prospectively ending the direct sellers' exemption as of the effective date of this section.

Sec. 402. RCW 82.04.423 and 1983 1st ex.s. c 66 s 5 are each amended to read as follows:

(1) Prior to the effective date of this section, this chapter ((~~shall~~)) does not apply to any person in respect to gross income derived from the business of making sales at wholesale or retail if such person:

(a) Does not own or lease real property within this state; and

(b) Does not regularly maintain a stock of tangible personal property in this state for sale in the ordinary course of business; and

(c) Is not a corporation incorporated under the laws of this state; and

(d) Makes sales in this state exclusively to or through a direct seller's representative.

(2) For purposes of this section, the term "direct seller's representative" means a person who buys only consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells at retail, or solicits the sale at retail of, only consumer products in the home or otherwise than in a permanent retail establishment; and

(a) Substantially all of the remuneration paid to such person, whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked; and

(b) The services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such purposes for federal tax purposes.

(3) Nothing in this section ((~~shall~~)) may be construed to imply that a person exempt from tax under this section was engaged in a business activity taxable under this chapter prior to ((~~the enactment of this section~~)) August 23, 1983.

PART V

Business and Occupation Tax Preferences for Manufacturers of Products Derived from Certain Agricultural Products

person must repay the amount of taxes exempted under this section. Interest as provided in chapter 82.32 RCW applies to amounts due under this subsection (3)(b) until paid in full. A person is not required to repay taxes under this subsection with respect to property and services for which the person is required to repay taxes under RCW 82.08.--- (section 2, chapter 1 (ESSB 6789), Laws of 2010 1st sp. sess.).

(4) The definitions and requirements in RCW 82.08.--- (section 2, chapter 1 (ESSB 6789), Laws of 2010 1st sp. sess.) apply to this section.

(5) This section expires April 1, 2018.

PART XVII
Miscellaneous Provisions

NEW SECTION. **Sec. 1701.** If a court of competent jurisdiction, in a final judgment not subject to appeal, adjudges any provision of section 104(1)(c) of this act unconstitutional or otherwise invalid, Part I of this act is null and void in its entirety.

NEW SECTION. **Sec. 1702.** Part I of this act applies with respect to gross income of the business, as defined in RCW 82.04.080, including gross income from royalties as defined in RCW 82.04.2907, generated on and after June 1, 2010. For purposes of calculating the thresholds in section 104(1)(c) of this act for the 2010 tax year, property, payroll, and receipts are based on the entire 2010 tax year.

NEW SECTION. **Sec. 1703.** Except as provided in section 202 of this act, section 201 of this act applies to tax periods beginning January 1, 2006.

NEW SECTION. **Sec. 1704.** Sections 402 and 702 of this act apply both retroactively and prospectively.

NEW SECTION. **Sec. 1705.** In accordance with Article VIII, section 5 of the state Constitution, sections 702 and 1704 of this act do not authorize refunds of business and occupation tax validly collected before July 1, 2010, on amounts received by an individual from a

corporation as compensation for serving as a member of that corporation's board of directors.

NEW SECTION. **Sec. 1706.** Section 402 of this act does not affect any final judgments, not subject to appeal, entered by a court of competent jurisdiction before the effective date of this section.

NEW SECTION. **Sec. 1707.** Except as provided in section 1701 of this act, if any provision of this act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected.

NEW SECTION. **Sec. 1708.** Except as otherwise provided in this act, this act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and takes effect May 1, 2010.

NEW SECTION. **Sec. 1709.** Parts III and XIII and sections 101 through 106, 108 through 112, 501 through 503, 505, 507, 510 through 514, 516 through 519, 901, 903 through 911, and 1201 of this act are necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and take effect June 1, 2010.

NEW SECTION. **Sec. 1710.** Sections 106, 901, and 1201 of this act expire July 1, 2010.

NEW SECTION. **Sec. 1711.** Sections 503, 505, and 514 of this act expire June 10, 2010.

NEW SECTION. **Sec. 1712.** Sections 504, 506, and 515 of this act are necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and take effect June 10, 2010.

NEW SECTION. **Sec. 1713.** Parts VI, VII, and XIV and sections 107, 702, 902, and 1202 of this act are necessary for the immediate

APPENDIX B

STATE OF WASHINGTON
DEPARTMENT OF REVENUE

July 2, 2010

Bill Metzinger, Chief Financial Officer
1 Dot Way
PO Box 192
Mount Sterling IL 62353-0192

RE: Dot Foods, Inc. Refund Request

Dear Mr. Metzinger:

Why you are receiving this letter
Recently you requested a refund of Wholesaling B&O tax on behalf of Dot Foods, Inc. (Dot Foods) based on the Supreme Court decision Dot Foods, Inc. v Department of Revenue, Docket No. 81022-2. In that decision, the court ruled that Dot Foods was entitled to the direct sellers' exemption found under RCW 82.04.423 with respect to the consumer products that it sold in Washington. On behalf of Dot Foods, you submitted a request for refund of Wholesaling B&O tax for the period January 2005 through August 2009. This letter is in response to that request.

Legislative changes that affect Dot Foods
In April 2010 the Washington legislature passed 2ESSB 6143 which retroactively amends RCW 82.04.423 to conform to the original intent of the legislature and prospectively ends the direct sellers' exemption. In Section 402 of that bill it defines a direct sellers' representative as:

> "a person who buys *only* consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells at retail, or *solicits the sale at retail of, only consumer products in the home or otherwise than in a permanent retail establishment.*" (Emphasis added)

As Dot Foods sold non-consumer products and many of those products were eventually sold at permanent retail establishments, Dot Foods does not qualify for the direct sellers' exemption found under 82.04.423 as amended by 2ESSB 6143.

Section 1706 of 2ESSB 6143 clarifies the retroactive application of this bill. It states:

> "Section 402 of this act does not affect any final judgments, not subject to appeal, entered by a court of competent jurisdiction before the effective date of this section."

The retroactive application of the bill does not affect the periods included in the Dot Foods Supreme Court decision. Specifically, it will not apply to the periods from January 2000 through April 2006.

Denial of a portion of refund request

The Dot Foods refund request includes the periods January 2005 through August 2009. For the periods outside the litigation resulting in the court decision, your refund request is denied based on the retroactive application of 2ESSB 6143. Specifically, the refund request for Wholesaling B&O tax for the periods from May 2006 through August 2009 is denied.

Additional information required

For the periods within the litigation, please continue to work with Senior Assistant Attorney General Cam Comfort regarding Dot Foods refund claims. Furthermore, with respect to the period January 2005 through April 2006, since Dot Foods refund claims has been preserved as part of the litigation, your administrative refund request for that period also is denied.

If you have questions you may contact me at (360) 902-7172.

Sincerely,

Andy Van Gerpen
Department of Revenue

APPENDIX C

STATE OF WASHINGTON
DEPARTMENT OF REVENUE

EXAMINER'S DETAIL OF DIFFERENCES AND INSTRUCTIONS TO TAXPAYER

Dot Foods Inc

Registration Number 601 197 196

A desk examination has been performed on your account for the period of September 1, 2009 through April 30, 2010.

Business Activities

Your business activities in Washington State during the examination period included sales of consumer and non-consumer products.

This assessment is limited in scope to the information provided on your Washington State excise tax returns. It is qualified to the extent that it includes taxes reportable on the excise tax return only. Amounts reportable on other tax returns or by other means are not included in this assessment.

As the examination did not include a detailed audit of the business' accounting records, this assessment is qualified to allow a future audit covering all areas of possible taxation within the statutory period as addressed in Revised Code of Washington (RCW) 82.32.050. The Department of Revenue reserves the right to assess any other tax due or tax credit found at a later date for the time period covered by this assessment.

References

The instructions provided in this report may address the application of the Revised Code of Washington (RCW); the Washington Administrative Code (WAC); the Washington Tax Decisions (WTD); and/or the Excise Tax Advisories (ETA) to the audit schedules. They constitute "specific written instructions" within the meaning of RCW 82.32.090. All authoritative references are available at the Department's Internet website: http://dor.wa.gov.

The following abbreviation may also be used in this report: business and occupation (B&O) tax.

Schedule 1 – Summary of Tax Adjustments by Classification

This schedule summarizes the tax difference as calculated on supporting Schedule 2.

Schedule 2 - To Assess Wholesaling Business and Occupation Tax

Pursuant to RCW 82.04.423 and WAC 458-20-246, which for excise tax purposes has the same effect as the Revenue Act itself (RCW 82.32.300) the B&O tax does not apply to gross income of out-of-state vendors with respect to wholesale or retail sales of "consumer products" into Washington State to or through a direct seller's representative. To qualify for the B&O tax exemption, all such sales into Washington must be made exclusively through the representative under a written agreement.

A "consumer product" is any article of tangible personal property, or component part thereof, of the type sold for personal use or enjoyment. The term includes only those kinds of items of tangible personal property which are customarily sold at stores, shops, and retail outlets open to the public in general. It includes home furnishings, clothing, personal effects, household goods, food products, and similar items purchased for personal use or consumption. The term does not include commercial equipment, manufacturing items, industrial use products, and the like, including component parts thereof.

A direct seller's representative is a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale. Sales or the solicitation of sales by the direct seller's representative must not be made in a permanent retail establishment.

To be considered a direct seller's representative the following conditions must be met:

- The remuneration paid for the performance of services is directly related to sales or other output, rather than the number of hours worked.
- Services are performed pursuant to a written contract between the representative and the out-of-state vendor for whom the services are performed. This contract must provide that the representative will not be treated as an employee for federal tax purposes.

This exclusion does not apply if any of these conditions exist:

- The vendor maintains an inventory of goods in Washington.
- The vendor owns or leases real property in Washington.
- The vendor is represented by any employee, agent, or other representative in Washington.
- The vendor is incorporated under the laws of Washington State.

Although such sales may be exempt from the B&O tax, an out-of-state vendor is required to collect and remit the retail sales or use tax to Washington if the vendor regularly solicits or makes retail sales of "consumer products" in Washington through a direct seller's representative as defined above.

As of January 1, 2000, WAC 458-20-246 was revised to reiterate the expressed requirements of RCW 82.04.423. This includes the limitation that consumer products ultimately sold in permanent retail establishments are not eligible for the exemption. Thus, regardless of whom the representative sells to, the retail sale of the product must take place either in the buyer's home or in a location that is not a permanent retail establishment.

In September 2009 the Washington Supreme Court ruled that Dot Foods was entitled to the direct sellers' exemption found under RCW 82.04.423 with respect to the consumer products that it sold in Washington. On the excise tax returns filed by Dot Foods from September 2009 through April 2010, Dot Foods has taken the deduction allowed for direct sellers.

In April 2010 the Washington legislature passed 2ESSB 6143 which retroactively amends RCW 82.04.423 to conform to the original intent of the legislature and ends the direct sellers' exemption. In Section 402 of that bill it defines a direct sellers' representative as:

> "a person who buys *only* consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail

> establishment, or who sells at retail, or *solicits the sale at retail of, only consumer products in the home or otherwise than in a permanent retail establishment.*" (Emphasis added)

As Dot Foods sold non-consumer products and many of those products were eventually sold at permanent retail establishments, Dot Foods does not qualify for the direct sellers' exemption found under 82.04.423 as amended by 2ESSB 6143.

Section 1706 of 2ESSB 6143 clarifies the retroactive application of this bill. It states:

> "Section 402 of this act does not affect any final judgments, not subject to appeal, entered by a court of competent jurisdiction before the effective date of this section."

The retroactive application of the bill does not affect the periods included in the Dot Foods Supreme Court decision. Specifically, it does not apply to the periods from January 2000 through April 2006. Since the periods from September 2009 through April 2010 are not included in the litigation, the retroactive application of the bill does apply to these periods so the direct sellers' deduction has been disallowed.

Wholesaling B&O tax has been assessed on gross income from wholesale sales of consumer and non-consumer products.

Penalties

RCW 82.32.090 imposes a 5 percent assessment penalty on tax assessments. The 5 percent assessment penalty will only be applied if the tax that is found to be due was substantially underpaid and if the amount of underpaid tax is at least $1,000. The law defines "substantially underpaid" to mean that the taxpayer has paid less than 80 percent of the amount of tax determined to be due by the Department.

You have been assessed the 5 percent assessment penalty.

Closing Comments

The adjustments were discussed with Jim Tracy, Senior Vice President, on July 1, 2010.

If there are any questions regarding these adjustments or if additional information is needed, contact either Debora Hadley, Senior Excise Tax Examiner, telephone number (360) 902-7072; or Andy Van Gerpen, Tax Administration Manager, telephone number (360) 902-7172; prior to the due date shown on the assessment. Copies of all authoritative references cited in this report may be downloaded from the Department's Internet website: http://dor.wa.gov.

RCW 82.32.050 imposes interest on the tax due before any payments are made. Full payment of the tax, penalties and interest must be made by the due date to avoid additional interest and penalties. The penalty imposed will be 15 percent of the tax due if the payment is not made by the due date.

For procedures to file a petition for appeal, refer to the 'File and Pay Taxes' section on the Department's website.

You must file an appeal (or an extension) within 30 days of the date the assessment was issued in order for the appeal to be received timely. If filed timely, the assessment does not have to be paid while awaiting review. Interest will accrue on any unpaid amount.

When an appeal is not filed or postmarked on time, you must first pay the assessment and then file an appeal seeking a refund within the statute of limitations (see WAC 458-20-229). Additional information is contained in WAC 458-20-100.

RCW 82.32.090 and WAC 458-20-228 provide that a 10 percent penalty may be assessed in addition to any tax found due if the Department of Revenue finds that a deficiency resulted from the disregard of specific written reporting instructions. A taxpayer will be considered as having disregarded specific written instructions when the Department has specifically advised the taxpayer that failure to act in accordance with those instructions may result in the 10 percent negligence penalty being imposed.

The taxpayer will not be considered as having disregarded such written instructions if the taxpayer has appealed the subject matter of the instructions and if the Department has not yet issued its final instructions or decision. The Department will not impose the negligence penalty upon any taxpayer that has made a good faith effort to comply with specific written instructions provided by the Department.

These instructions apply to tax asserted on Schedule 2 imposing tax due on sales of consumer and non-consumer products under the Wholesaling B&O tax classification. Failure to follow the written reporting instructions given for this schedule may cause the negligence penalty to be invoked.

Thank you for your cooperation and assistance.

Debora Hadley, Senior Excise Tax Examiner

Taxpayer Account Administration Division